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ACADEMIC PERSPECTIVES ON SALT

tax notes state

The Ordinary Diet of the Law: How to Interpret Public Law 86-272

by Darien Shanske and David Gamage



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In this installment of Academic Perspectives on SALT, the authors argue that a proper, fair reading of Public Law 86-272 should not involve expanding its coverage to protect business practices that differ from the practices that Congress specifically intended to protect at the time of the statute's enactment.

Indeed, in today's world, filled with legal complexity, the true test of federalist principle may lie, not in the occasional constitutional effort to trim Congress' commerce power at its edges, or to protect a State's treasury from a private damages action, but rather in those many statutory cases where courts interpret the mass of technical detail that is the ordinary diet of the law.¹

¹ *Egelhoff v. Egelhoff*, 532 U.S. 141, 160-61 (2001) (Breyer, J. dissenting) (internal citations omitted).

Public Law 86-272 is an important feature of the landscape of both state corporate income taxation and state tax policy more generally.² The Multistate Tax Commission is completing an important project on updating the guidance given to taxpayers regarding compliance with P.L. 86-272.³ We plan to discuss some key features of this planned guidance in a future article (or perhaps articles). But first we will discuss the overall interpretive rubric that should be used for P.L. 86-272.

I. Some Quick Background

P.L. 86-272 protects taxpayers from state income taxation if certain criteria are met.⁴ Those criteria include not having an office in the state and only selling tangible personal property. For purposes of the MTC project, the most important criterion is that a taxpayer is protected if it engages only in "solicitation" in the state.

However, the statute itself offers little direct guidance on what solicitation means. Nor is such guidance to be found in the legislative history. This has long been recognized as an important problem.⁵

² Just how important a feature is, in fact, a hard question to answer. See Dan R. Bucks et al., "Public Law 86-272: Still Bad Policy After 60 Years," *Tax Notes State*, Oct. 7, 2019, p. 13, 16-18. For a fuller discussion — and critique — of P.L. 86-272, see Michael T. Fatale, "Federalism and State Business Activity Tax Nexus: Revisiting Public Law 86-272," 21 *Va. Tax Rev.* 435 (2002).

³ Multistate Tax Commission, "P.L. 86-272 Statement of Information Work Group."

⁴ 15 U.S.C. section 381.

⁵ See, e.g., Paul J. Hartman, "State Taxation of Corporate Income From a Multistate Business," 13 *Vand. L. Rev.* 21, 47 (1959).

Today, the primary source of authority for interpreting solicitation is the 1992 Supreme Court opinion in *Wrigley*⁶ written by Justice Antonin Scalia. In that opinion, Scalia largely eschewed legislative history and instead started with a dictionary “to ascertain the fair meaning” of solicitation.⁷

Specifically, Scalia found that solicitation encompassed “those activities that are *entirely ancillary* to requests for purchases — those that serve no independent business function apart from their connection to the soliciting of orders — [in contrast to] those activities that the company would have reason to engage in anyway but chooses to allocate to its in-state sales force.”⁸ Scalia illustrated the distinction by way of examples, explaining that “employing salesmen to repair or service the company’s products is not part of the ‘solicitation of orders,’ since there is good reason to get that done whether or not the company has a sales force.”⁹

Yet now, in 2020, some repairs can be done over the internet. Should this change in technology mean that such in-state services do *not* go beyond solicitation?¹⁰ The result of such an interpretation would be to let technological advancements effectively expand the scope of “solicitation” and create an ever larger “tax free” zone. The MTC guidelines are premised on the notion that this is not the correct way to interpret the law. Accordingly, one of the proposed guidelines explains that if “the business regularly provides post-sale assistance to in-state customers (i.e., advice on how to use a product after the product has been delivered to the customer) via

either electronic chat or email that customers initiate by clicking on an icon on the business’s website,” then the business loses the protection of P.L. 86-272.¹¹

II. A Matter of Interpretation

There is another way of looking at matters, of course. We just characterized the MTC approach as not letting technology expand the concept of solicitation. Others take the perspective that the MTC approach is narrowing the legitimate reach of P.L. 86-272.¹² No doubt there can be arguments in specific cases about what constitutes solicitation, but we see this counterargument as primarily a legislative intent or purpose-based argument. The argument has some appeal. Congress meant to set up a minimum standard of nexus with P.L. 86-272 and narrowing the definition of “solicitation” would seem to puncture this minimum.

However, this surface appeal disappears upon closer inspection. This is for reasons that we will now explain.

First, Congress did not, in fact, write a statute that imposed a minimum standard. Rather, Congress wrote a statute that created a minimum through a set of rules. That is, Congress passed specific protections — protections that traced then-current business practices that had come to Congress’s attention through court cases.¹³ Indeed, the statute Congress passed would not even protect the taxpayer at issue in the main Supreme Court decision that precipitated the

¹¹ MTC, “Statement of Information Concerning Practices of Multistate Tax Commission and Signatory States Under Public Law 86-272,” Example 2 (Feb. 14, 2020).

¹² See presentation by Philip Tatarowicz linked to in Amy Hamilton, “Tatarowicz Sharply Critical of MTC Project on P.L. 86-272,” *Tax Notes State*, Dec. 23, 2019, p. 1190, at slide 44 (“From an income tax nexus perspective, if the tools of efficiency created by E-Commerce are weaponized by States going wild to expand their tax reach, P.L. 86-272 will be emasculated; thus, turning away from Congressional intent.”); Christopher T. Lutz, “What to Do With Public Law 86-272,” *Tax Notes State*, Dec. 23, 2019, p. 1071, 1072 (“I’m not so sure the MTC’s Uniformity Committee is really geared to faithfully construe the text and purpose of P.L. 86-272”); David W. Bertoni, David Swetnam-Burland, and Jamie Szal, “Crossfire Hurricane: Perils in a Post-Wayfair World,” *Tax Notes State*, Mar. 16, 2020, p. 937, 942 (“Under the mantra of bringing P.L. 86-272 into the modern era, the working group of the MTC has lost sight of the fundamental purpose of this federal statute and the protection it provides.”).

¹³ See, e.g., H.R. Rep. No. 86-936 at 1 (1959). The three cases are: *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450, 454 (1959); *Brown-Forman Distillers Corp. v. Collector of Revenue*, 234 La. 651 (1958); *International Shoe Co. v. Fontenot*, 236 La. 279 (1958).

⁶ *Wisconsin Department of Revenue v. William Wrigley Jr. Co.*, 505 U.S. 214 (1992).

⁷ *Id.* at 223-24.

⁸ *Id.* at 228-29.

⁹ *Id.* at 229.

¹⁰ This is also why the word “within” in P.L. 86-272 cannot bear the interpretive weight that some commentators place upon it. See Martin I. Eisenstein and David W. Bertoni, “Wayfair Misused: States and Cities Seek to Expand Their Tax Powers,” *Tax Notes State*, Dec. 16, 2019, p. 891, 896-97. To be sure, the nonprotected activities must occur *within* the state, but when, for example, an item is repaired in the state by means of the internet there is a powerful argument that *that* activity is in the state.

whole crisis — *Northwestern Portland*. This is because a taxpayer loses the protection of P.L. 86-272 if it maintains an office in the state, and the taxpayer in *Northwestern Portland* had an office in the taxing state.

The version of the bill referred out of the Senate Finance Committee did protect businesses with an office in state if they just engaged in solicitation,¹⁴ and would have covered the *Northwestern Portland* fact pattern. Yet the bill was amended on the Senate floor and, by a vote of 65-29, this provision was eliminated.¹⁵ Given that Congress pared the law back not even to cover the three central business scenarios before it, but rather only two, it is non-persuasive to argue that Congress intended the bill to protect further business patterns then completely unimaginable.

Second, a corollary of this point is that it is generally not proper statutory interpretation to argue that Congress's intent to protect specific business patterns should apply to other arguably similar business patterns, just because doing otherwise would make the statute less relevant to modern circumstances. For instance, imagine that Congress passed a law to protect buggy whip manufacturers and never repealed that law. Would that mean that there is now an interpretative imperative to protect other transportation-related manufacturers? No!¹⁶ The goal of protecting buggy whip manufacturers might well have been motivated by special interest concerns of the time or a desire to slow the transitionary displacement caused by technological changes (like the spread of automobiles). Put another way, just because Congress passed a statute 60 years ago with two fact patterns in mind, and with the language of the statute reflecting concerns related to those two fact patterns, in no way implies that the statute

was meant to serve a broader purpose. If those fact patterns are far less important today, then it should be up to Congress to decide how to update the statute or whether to do so at all.

Third, the legislative history indicates that Congress did not intend P.L. 86-272's protections to extend to near substitutes of the specific forms of business explicitly protected, including a case rather analogous to the ones we are now considering. That is, in its report on P.L. 86-272, the Willis Committee explained that it did not consider that "Operation of mobile stores in the State" was an activity that was intended to be protected by the statute.¹⁷ To be sure, the Willis Committee report postdates the enactment of P.L. 86-272, but it is fairly close in time and the whole point of this section of the report was to consider whether Congress should retain P.L. 86-272.¹⁸ A mobile store in the state would seem to be a fair 1960s description of what the modern internet effectively enables.

Fourth, the problem Congress aimed to legislate against with P.L. 86-272 has mostly gone away with time, which further weighs against a sweeping interpretation of the statute. Congress legislated P.L. 86-272 out of fear that the Supreme Court might not set an appropriate minimum for nexus.¹⁹ Today, that fear is unfounded. In fact, the protections offered by current constitutional jurisprudence are often greater than those offered by P.L. 86-272. Most obviously, this is because the constitutional "substantial nexus" standard protects all taxpayers, even sellers of services, from all taxes.

But even as to just the income tax the constitutional standard will often be higher. A relatively small taxpayer can lose the P.L. 86-272 protection for minor in-state activities, such as engaging in \$10,000 in sales that are not fulfilled out of state. This level of nexus is probably not

¹⁴ S. Rep. No. 86-658 at 6 (1959).

¹⁵ 105 Cong. Rec. 16470, 16477 (1959).

¹⁶ And so, at least as to P.L. 86-272, we agree with Bertoni et al. that "the words of a tax statute enacted in the 1950s must have the meaning that was intended when it was enacted, and not be given some gloss that rests on a radically different economy and modalities of commerce that came into existence many decades later." Bertoni, Swetnam-Burland, and Szal, *supra* note 12, at 943. Perplexingly, the authors claim that this argument indicates that there is something amiss in the MTC's project. This is apparently because of their overreading of the word "within." See *supra* note 10. Again, we argue that extending solicitation to include interactive websites is to give an old statute a radical new gloss and not the reverse.

¹⁷ H. Rep. No. 88-1480 at 427 (1964).

¹⁸ Treating this report as part of P.L. 86-272's legislative history is quite common. See, for example, Tatarowicz, *supra* note 12, slide 53.

¹⁹ See, e.g., S. Rep. 86-658 at 4; and H. Rep. No. 88-1480 at 438.

going to qualify as substantial under *Wayfair*. Moreover, many states have bright-line factor standards that are comfortably above the constitutional minimum.²⁰

Further, the Court in *Wayfair* made clear that *Pike* balancing²¹ applies on top of the substantial nexus test.²² Thus, a taxpayer confronting a particularly onerous state tax regime today has another available remedy. And because *Pike* balancing is a balancing test, burdens that loom larger for smaller businesses will be harder to justify. With the mischief Congress tried to solve through P.L. 86-272 thus largely resolved by subsequent judicial decisions, purpose-based arguments for expanding P.L. 86-272 have little analytic purchase.

We think that this is the primary significance of *Wayfair* as to P.L. 86-272. But *Wayfair* is also relevant in that not one member of the Court in *Wayfair* had anything nice to say about the formal, physical presence test from *Quill*.²³ Indeed, the majority, in a key passage, discussed the importance of “virtual contacts” in potentially creating nexus in the modern economy.²⁴ The dissent did not dispute this so much as argue that the great increase in e-commerce indicates that the Court should not intercede because of the unpredictable result of fixing its error. Note that from our perspective, “modernizing” P.L. 86-272 so it would exempt new forms of commerce

would be to repeat the sins of *Quill* and, also, of *Wayfair* as understood by the dissent.²⁵

Fifth, a fundamental ground rule in our constitutional system is that preemptions of traditional state powers should be construed narrowly.²⁶ It is true that much of the development of this doctrine postdates P.L. 86-272 (not that this has stopped the Court from applying it to earlier statutes), but there was definitely precedent to this effect before 1959.²⁷ A canon is only an interpretive guide that can make more or less sense to apply in a given context. Yet here we would argue this canon is particularly apt because it correctly addresses a deep structural issue underlying our federal system.²⁸ Through the lens of this canon, Congress should be understood as having made a limited incursion into state taxing power with P.L. 86-272, to solve a then-current problem. The alternative view has Congress creating a shelter from state taxation limited only by the ingenuity of tax lawyers to analogize current business models to the ones before Congress in 1959. It is useful to remember here that Congress could have, but did not, pass a broad nexus standard and thus that this canon is consonant with the text of the statute.

Note that our argument relying on the canon against preemption here is, in a sense, subtle. In

²⁰ It is thus wholly appropriate for new guidance from the MTC to include its model factor presence standard as an addendum. Brian Hamer of the MTC makes the same point. See Hamilton, “Factor Presence Nexus Thresholds Way to Protect Small Sellers,” *Tax Notes State*, Mar. 16, 2020, p. 992.

²¹ *Pike v. Bruce Church Inc.*, 397 U.S. 137 (1970).

²² *South Dakota v. Wayfair Inc.*, 585 U.S. ___, 138 S. Ct. 2080, 2099 (2018). For further discussion, see Adam Thimmesch, Darien Shanske, and David Gamage, “*Wayfair*: Substantial Nexus and Undue Burden,” *State Tax Notes*, July 30, 2018, p. 447.

²³ *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992).

²⁴ *Wayfair*, 138 S. Ct. at 2095 (“A virtual showroom can show far more inventory, in far more detail, and with greater opportunities for consumer and seller interaction than might be possible for local stores. Yet the continuous and pervasive virtual presence of retailers today is, under *Quill*, simply irrelevant. This Court should not maintain a rule that ignores these substantial virtual connections to the State.”).

²⁵ *Id.* at 2104 (“The Court is of course correct that the Nation’s economy has changed dramatically since the time that *Bellas Hess* and *Quill* roamed the earth. I fear the Court today is compounding its past error by trying to fix it in a totally different era.”) (Roberts, C.J., dissenting).

²⁶ See, e.g., *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947) (“We start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress.”). See also *California State Board of Equalization v. Sierra Summit Inc.*, 490 U.S. 844, 851-52 (1989) (“Although Congress can confer an immunity from state taxation, we have stated that [a] court must proceed carefully when asked to recognize an exemption from state taxation that Congress has not clearly expressed.”) (internal citations and quotation marks omitted); see also *Florida Department of Revenue v. Piccadilly Cafeterias Inc.*, 554 U.S. 33, 48, 50 (2008) (following *Sierra Summit*). For further discussion, see Shanske, “States Can and Should Respond Strategically to Federal Tax Law,” 45 *Ohio N.U. L. Rev.* 543 (2019).

²⁷ It is also true that the canon has not been applied consistently, but that does not mean that it should not be. For a persuasive argument to this effect, see Ernest A. Young, “The Ordinary Diet of the Law’: The Presumption Against Preemption in the Roberts Court,” 2011(1) *Sup. Ct. Rev.* 253, 344 (Jan. 2012) (“The presumption against preemption may be the last best hope for preserving a meaningful measure of state autonomy in our constitutional system.”).

²⁸ Following Llewellyn, the key to applying a canon correctly is “situation sense.” Karl Llewellyn, “Remarks on the Theory of Appellate Decision and the Rules or Canons About How Statutes Are to Be Construed,” 3 *Vand. L. Rev.* 395, 401 (1950).

Heublein, the Supreme Court's first P.L. 86-272 case, this presumption was used to avoid an expansive interpretation of P.L. 86-272.²⁹ In *Wrigley*, the states argued that this same presumption should lead to solicitation being interpreted narrowly. Scalia rejected that argument because, as to solicitation, Congress did clearly intend to preempt the states and so what was required was only a fair interpretation of what Congress actually wrote. But the situation before us today is more like *Heublein* than *Wrigley*. This is because at least some of the activities that taxpayers engage in through their websites are plainly more than entirely ancillary to solicitation and have been understood to be such since well before *Wrigley*. Thus, the critics of updating the guidelines are, as in *Heublein*, arguing for an extension of the protection offered by P.L. 86-272.

III. Conclusion

None of the foregoing necessarily supports the details of the MTC's approach. We will thus return to analyzing those details in a future article or articles. Our goal here has been to clear away the interpretive underbrush. P.L. 86-272 is a poorly drafted, 60-year-old statute that specifically protects 60-year-old business practices. Consequently, we have argued here that a proper, fair reading of the statute should not involve expanding its coverage to protect current business practices that differ from those Congress specifically meant to protect when enacting P.L. 86-272. ■

²⁹ *Heublein Inc. v. South Carolina Tax Commission*, 409 U.S. 275, 281-82 (1972).

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